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SUBJECT: BRAZIL: NEW SCANDAL COULD MEAN ANOTHER LOST YEAR  
FOR GOVERNMENT

REF: BRASILIA 00207

¶1. (SBU) Summary: The latest scandal to engulf the Lula government was unleashed January 13 when influential daily Estado de Sao Paulo took advantage of one of the government's most highly touted clean-government initiatives, its transparency web portal, to report on the exponential increase in use of government credit cards for alleged inappropriate purchases by thousands of government officials, including by several Ministers, during Lula's presidency. The government initially reacted to the news reports by sacrificing its most conspicuous spender, Special Secretary for Promotion of Racial Equality Matilde Ribeiro, but the scandal quickly careened out of control before the government found its footing and went on the offensive to stave off further efforts by the opposition to claim additional victims. Since the revelations, the opposition has been engaged in a struggle for control of the congressional investigative committee (CPI) that will soon convene to investigate the abuse of government credit cards, and failing that, will look for ways to pressure the government to release its records so they can guarantee that a steady trickle of potentially salacious revelations will weaken the government during a year of state and municipal elections. Depending on the scope of the investigation some believe this scandal could have legs and could stall the government's legislative agenda, including the government's tax reform plan, for the year. Recent polls, however, indicate that Lula's popularity remains undiminished, suggesting that short of any blockbusters, he will, as in the past, personally weather any potential problems arising from new revelations. End Summary.

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Free for All: From Beach Umbrellas to Tapioca  
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¶2. (U) On January 13, Estado de Sao Paulo reported that since Lula took office in 2003, his administration's government credit card expenditures have gone up by more than 2000%, from R\$3.6 million (about US\$2 million) in 2002, the last year of Fernando Henrique Cardoso's government to R\$78 million (US\$45.5 million) in 2007. About 75% of those expenditures, or R\$58 million (US\$33.7 million), resulted from largely untraceable cash withdrawals at ATM machines. The remainder, or what can be accounted for in the government's transparency portal, was spent on a vast range of purchases, many verging on the absurd. Since January 13,

the media has had a field day reporting on the more than 7000 public employees who use the 11,000-13,000 government credit cards, detailing purchases that range from multiple no-bid car rentals with the same company, to video rentals, to purchases at flower shops, butchers, wine shops, beauty salons, duty free shops, local markets known for selling pirated goods, and many more. One minister used his credit card to pay for R\$8 (US\$4.50) worth of tapioca, leading Planning Minister Paulo Bernardo to ridicule a possible Congressional investigation by dubbing it the "Tapioca CPI".

13. (U) The most egregious spender, Special Secretary for Policies to Promote Racial Equality Matilde Ribeiro, at least the ninth minister to be forced out by scandal since the start of Lula's presidency, got the hook because, according to analyst Andre Miranda from the political consulting firm PATRI, the government thought it could contain the damage by sacrificing her. She apparently spent at least R\$171,500 (US\$99,000) in 2007 with the government card on a variety of unauthorized transactions, including purchases at duty free shops and bars and restaurants during her vacations. As a low-key minister and someone outside Lula's circle of key advisers, Miranda stated, she was expendable (reftel). Other Ministers in the spotlight, such as Sports Minister Orlando Silva, have been let off the hook by agreeing to pay back about R\$30,000 (US\$17,000) in personal expenditures.

14. (U) Despite the offering of Ribeiro as a sacrificial lamb, the opposition called for a CPI to look into the government's alleged abuses. The opposition is demanding at least one of the two important positions in a CPI, either that of president or rapporteur, which the government so far has

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resisted. Some in the opposition are also attacking the government for its refusal to allow the CPI to look at Planalto Palace's (the Office of the Presidency) use of the card, citing security concerns. According to a Veja investigative report, the ten biggest spending officials within Planalto accounted for more than R\$11.6 million (US\$ 6.7million) in purchases since 2003.

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The "Mistakes Were Made" Defense  
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15. (U) After scapegoating Ribeiro, the government's new defense focused on admitting that mistakes were made, that some excesses were committed, that these would be investigated and corrected, but that the vast majority of expenditures amounted to nothing more than administrative mistakes, due to unclear rules governing the use of the cards, a situation for which no one was to blame. Federal Deputy Nilson Mourao (Worker's Party- Acre), who will likely be appointed to the CPI, reflected the government's talking points when he told Poloff that this was a media-driven "scandal", and that he would focus his time in the CPI to making the necessary technical changes in the regulations. Various prominent ministers have stepped into the fray to defend the government as well. Both Comptroller General Jorge Hage and Justice Minister Tarso Genro have aggressively pursued this line of argument in the press, arguing that, if anything, the administration should be given credit for being as transparent as it was in creating the portal that allowed the press to report on these excesses.

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Government and PT go on the Offensive  
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16. (U) Aside from the government's "mistakes were made" defense, it also mounted a political offensive, first by opening up the Congressional inquiry to cover expenditures going back to 1998, the middle of Fernando Henrique Cardoso's government, and having the Worker's Party contingent in the

Sao Paulo State legislative assembly attempt to open up an inquiry in Sao Paulo against current Governor and possible Brazilian Social Democracy Party (PSDB) presidential candidate in 2010, Jose Serra. Taking aim at the main opposition party, powerful minister Dilma Rousseff compared the government's expenditures against both Cardoso's record and Serra's record. Although the card did not come into use until the last year of Cardoso's government, the government succeeded in making argument that expenditures using "contas tipo B" (bank accounts that can be used to pay by check by a limited number of government officials) during the Cardoso era should be included in the probe. Counting those expenditures, the Lula government can compare itself favorably with the Cardoso government (R\$176 million, or US\$102.4 million, in 2007 versus R\$233 million, or US\$ 135.6 million, with both the credit card and the B accounts in 2002). They further succeeded in cutting a deal with the PSDB to exclude the presidency's expenditures from the investigation, although analyst Miranda questioned if the deal could hold for long. Furthermore, according to most press accounts, Planalto is quite openly insisting on loyalists to make up its portion of the CPI, to ensure that no one goes off the reservation, as happened with the tough investigation that followed the "CPI dos Correios" headed by Senator Delcidio do Amaral (PT-MS) and Federal Deputy Osmar Serraglio (PMDB-PR).

17. (U) On February 12, in light of reports by Folha de S. Paulo that his administration had spent more than R\$ 108 million using government-issued debit cards, Governor Serra suspended the use of such cards for cash withdrawals and ordered an internal review of spending practices. The PT leader in the Legislative Assembly, Simon Pedro, sought to establish a CPI. However, PT State Deputy Rui Falcao told Poloff on February 15 that the PSDB and its allies had the votes to block any legislative investigation. Instead, Falcao has filed complaints with the state Public Ministry (prosecutor's office) asking for a criminal investigation and especially demanding that the state government publish its expenditure reports on the internet as the federal government

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does.

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Allied Parties Stand to Gain the Most  
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18. (U) Andre Miranda sees the Brazilian Democratic Movement Party (PMDB) and other parties in the allied base as the chief beneficiaries of the scandal. A CPI is an excellent opportunity for the PMDB, the PT's main coalition partner, to extract concessions, such as key government posts, from the government. The PMDB's less than loyal way of doing business means that many of its members will not hesitate to abandon the government if they sense the government is on the losing side of an argument and will pounce if they sense the government is weak. The fact that the government appears to be moving ahead with its tax reform plan, according to Miranda, gives the PMDB even more leverage over the government.

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Potential Minefield Ahead  
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19. (U) Although polls show that Lula is as popular as ever and the government appears to have reached some kind of agreement to limit the scope of the investigation, a number of obstacles remain for the government to overcome over the next few months. First, the opposition remains ready and willing to push for a separate Senate-only CPI, where the proportion of opposition members would mean a more favorable balance. Second, although not an incredibly important or influential entity, the Tribunal de Contas (TCU, the government's accounting office) has launched its own inquiry,

the findings of which, when released, could lead to a new round of embarrassing news stories unfavorable to the government. A potential source of embarrassment could come when the CPI or the TCU asks for receipts for purchases made using cash withdrawals. The possibility that these may not have been kept, or that if they were will reveal more abuses, could result in a new round of unfavorable press coverage. Third, the independent Public Ministry could launch its own probe. Fourth, if Planalto stonewalls the CPI, the Brazilian Supreme Court (Supremo Tribunal Federal-STF) could choose to get involved and demand an opening of the presidency's records. Public remarks by STF justices Celso de Mello and Marco Aurelio Mello attacking the notion that the presidency can keep its records secret suggest they could continue the federal judiciary's increasingly activist tendency to rule on political issues, as demonstrated in their "mensalao" and the party switching decisions.

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Comment: Another Lost Year?  
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¶10. (SBU) Lula appears to be as popular as at any time since the beginning of his presidency in 2003, and the government seems to be succeeding in its counteroffensive. It is not, however, out of the woods yet. Even with a government-controlled CPI, once one is established all bets are off, particularly in an election season. Any agreement to keep the presidency's records secret could break easily and the opposition and press can probably continue to find enough information to create problems for at least the worst offenders, even if the public buys into the government's defense and agrees that the majority of the spending was legitimate, if badly regulated. Even if nothing coming out of a CPI is likely to damage Lula personally, it could continue to erode the PT's reputation going into important municipal elections this year that could have national repercussions in 2010, claim additional victims within the government, and would probably make the government's efforts to advance its agenda nearly impossible. The government, which agreed to the CPI in order to co-opt it from the opposition, may have opened a Pandora's Box it may not be able to close before more damage is done. End Comment.

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